ST 01-0155-GIL 08/13/2001 FARM MACHINERY AND EQUIPMENT

Machinery and equipment that is used primarily (over 50% of the time) in production agriculture or for use in State or Federal agricultural programs may be purchased free from tax under the farm machinery and equipment exemption. 86 Ill. Adm. Code 130.305. (This is a GIL).

August 13, 2001

Dear Xxxxx:

This letter is in response to your letter dated June 29, 2001. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be found on the Department's website at http://www.revenue.state.il.us/legalinformation/regs/part1200.

In your letter, you have stated and made inquiry as follows:

Hi my name is Carolyn and I work in the tax and audit department of COMPANY. COMPANY **manufacture's, sells and leases golf cars, utility vehicles, and tractors and turf equipment.** I had written and sent this letter (April 18,2001) and in response was sent copies of information from the Internet. This did not answer or clear up our questions. We had already obtained and read this information from the Internet. I would like to ask a few tax questions related to the sale and rental of golf cars and utility vehicles in an on going effort to keep current tax facts. I sincerely appreciate any time you can take to answer the following questions.

1. A) What is the tax status? (taxable/non-taxable) (Are resale/exemption certificates allowed from) each of the following?
   B) What form(s) (is the multijurisdiction form excepted) are required for each of the following:
   - Farms
   - Repair Labor
   - Freight
   - Service Contracts
   - Municipalities (School, gov't, Hospitals, entities)
   - Non-Profit/charities
   - Churches
   - Golf course/clubs for resale/rental
   - Golf course/clubs for utility/turf equipment
   - Parts for repair on the sale/rentals items of our customers

2. This question will be in the form of an example. If state AA buys from us and we ship to customer (i.e. phone sales, Internet, traveling sales rep) in your state for them may we accept their states resale certificate or do they need one from your state? If state AA buys from us and we ship to one of their business location in your state for resale may we accept their states resale certificate or do they need one from your state?

3. How many years' back does your state allow for a tax credit to be given?

4. Is a tax credit allowed as a refund on a trade-in credit and/or is tax on net sale after trade-in allowance allowed on golf cars and utility vehicles? (i.e. Customer purchased golf car 3 years ago and is now allowed to trade-in on a new one. Cost of new less current value of old equals net cost. Would taxing the net cost be correct? Or issuing a credit for the trade-in including tax credit after the new purchase was made or agreed upon.)

5. What are the required or suggested renewal dates of resale and exemption Certificates (for audit reasons)?

6. How many digits/alpha does your resale and exemption certificates usually have and are there any identifying numeric/alpha beginning or ending characters?

7. COMPANY is considering innovative technology methods as an alternative to reduce paper use in are business. Please give us any information that relates to the use of scanning and like equipment with resale and exemption certificates. (i.e. are we legally required to keep on file the original certificates etc.)

Please send us any form and documentation that would be useful to us in our type of business. Again let me thank you for your help and wish you a nice Day.

Farm Machinery & Equipment

Machinery and equipment that is used primarily (over 50% of the time) in production agriculture or for use in State or Federal agricultural programs may be purchased free from tax under the farm machinery and equipment exemption. See the enclosed copy of 86 Ill. Adm. Code 130.305.

ATVs are primarily recreational in nature. Even though a farmer may, on occasion, use an ATV to drive around fields to check on crop conditions or livestock, such on-farm transport does not constitute production agriculture. Consequently, ATVs generally do not qualify for the farm machinery and equipment exemption. This has long been, and remains, the Department's position. However, farm utility vehicles that meet the requirements for the farm machinery and equipment exemption may qualify. Taxpayers who use GATORS, MULES, and utility vehicles in a qualifying manner may claim the exemption.

Service Contracts and Labor Costs Incurred When Repairing Equipment

Retailers' Occupation Tax and Use Tax do not apply to receipts from sales of personal services. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. For your general information we are enclosing a copy of 86

Ill. Adm. Code Part 140 regarding sales of service and Service Occupation Tax.

The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or, (4) Use Tax on cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See, 86 Ill. Adm. Code 140.101(f) enclosed. This class of registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self-assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. See 86 Ill. Adm. Code 140.109.

The taxability of maintenance agreements is dependent upon whether the charge for the agreement is included in the selling price of tangible personal property. If the charge for a maintenance agreement is included in the selling price of tangible personal property, that charge is part of the gross receipts of the retail transaction and is subject to Retailers' Occupation Tax liability.

No tax is incurred on the maintenance services or parts when the repair or servicing is completed.

If maintenance agreements are sold separately from tangible personal property, the sale of the agreement is not a taxable transaction. However, when maintenance services or parts are provided under the maintenance agreement, the company providing the maintenance or repair will be acting as a service provider under the Service Occupation Tax Act. The Service Occupation Tax Act provides that when a service provider enters into an agreement to provide maintenance services for a particular piece of equipment for a stated period of time at a predetermined fee, the service provider incurs Use Tax based upon its cost price of tangible personal property transferred to the customer incident to the completion of the maintenance service. See 86 Ill. Adm. Code 140.301(b)(3), enclosed.

Freight

As a technical proposition, handling charges represent a retailer's cost of doing business, and are consequently always included in gross charges subject to tax. See, 86 Ill. Adm. Code 130.410. However, such charges are often stated in combination with shipping charges. In this case, charges designated as "shipping and handling," as well as delivery or transportation charges in general, are not taxable if it can be shown that they are both separately contracted for and that such charges are actually reflective of the costs of shipping. To the extent that shipping and handling charges exceed the costs of shipping, the charges are subject to tax. As indicated above, charges termed "delivery" or "transportation" charges follow the same principle.

The best evidence that shipping and handling or delivery charges have been contracted for separately by purchasers and retailers are separate contracts for shipping and handling or delivery. However, documentation that demonstrates that purchasers had the option of taking delivery of the property, at the sellers' location for the agreed purchase price, plus an ascertained or ascertainable delivery charge, will suffice. If retailers charge customers shipping and handling or delivery charges that exceed the retailers' cost of providing the transportation or delivery, the excess amount is subject to tax.

Mail order delivery charges are deemed to be agreed upon separately from the selling price of the tangible personal property being sold so long as the mail order form requires a separate charge for delivery and so long as the charges designated as transportation or delivery or shipping and handling are actually reflective of the costs of such shipping, transportation or delivery. See subsection (d) of Section 130.415. If the retailer charges a customer shipping and handling or delivery charges that exceed the retailer's cost of providing the transportation or delivery, the excess amount is subject to tax.

Exempt Organizations

Organizations that make application to the Department of Revenue and are determined to be exclusively religious, educational, or charitable, receive exemption identification numbers (an "E" number). See the enclosed copy of 86 Ill. Adm. Code 130.2007. This number evidences that the Department recognizes the organizations as exempt from incurring Use Tax when purchasing tangible personal property in furtherance of their organizational purposes. If an organization does not have an E number, then its purchases are subject to tax. Organizations that are recognized as non-profit under Internal Revenue Code Section 501(c)(3), are not necessarily exempt organizations pursuant to Illinois tax law. Such organizations must obtain an Illinois "E" number to qualify. Please

be aware that only sales to organizations holding the E number are exempt, not sales to individual members of the organization.

These organizations are also allowed to engage in a very limited amount of retail selling without incurring Retailers' Occupation Tax liability. These limited amounts of selling are described in the enclosed copy of 86 Ill. Adm. Code 130.2005(a)(2) through (a)(4).

An exempt organization may engage in sales to members, noncompetitive sales, and certain occasional dinners and similar activities (two fundraisers a year) without incurring Retailers' Occupation Tax liability. In regards to sales to members, please note that the population to which sales are made is limited to persons specifically associated with that exempt organization and must be for the primary purpose of the selling organization. If such sales are made to the public at large the selling activity is subject to the Retailers' Occupation Tax. See section 130.2005(a)(2) through (a)(4). In determining whether the sales are for the primary purpose of the selling organization depends on the nature of the tangible personal property sold and how that tangible personal property is used. If an organization sells literature or other items of tangible personal property that would place them in competition with other religious bookstores, the sales generally would not be primarily for the purpose of the selling organization. However, sales of choir robes or like tangible personal property to members would generally be primarily for the purpose of the selling organization. Your client should not be cavalier in determining the nature of their sales as the Department cannot grant a binding determination in the context of a General Information Letter.

Further, if organizations engage in ongoing selling activities (such as Little League concession stands or sales of items in a thrift shop run by a church), they must also register with the Department as retailers, file returns and remit tax. Such organizations must provide their suppliers with Certificates of Resale when making purchases for resale. Illinois law requires a Certificate of Resale to contain the information set out in 86 Ill. Adm. Code 130.1405(b), enclosed. A valid Certificate of Resale must contain the following:

1. A short statement from the purchaser that the items are being purchased for resale;

2. The seller's name and address;

3. The purchaser's name and address;

4. The purchaser's signature and date of signing;

5. A sufficient identification or description of the items purchased for resale; and

6. One of the following:

   The purchaser's registration number with the Illinois Department of Revenue,

   The purchaser's resale number issued by the Illinois Department of Revenue, or

   A statement that the purchaser is an out-of-state purchaser who will sell only to purchasers located outside the State of Illinois

Sales for Resale

Illinois law requires a Certificate of Resale to contain the information set out in 86 Ill. Adm. Code 130.1405(b), enclosed. A Certificate of Resale is a statement signed by the purchaser that the property purchased by him is purchased for purposes of resale. Provided that this statement is correct, the Department will accept Certificates of Resale as prima facie proof that sales covered thereby were made for resale. In addition to the statement, a Certificate of Resale must contain:

1) The seller's name and address;
2) the purchaser's name and address;
3) a description of the items being purchased for resale;
4) purchaser's signature, or the signature of an authorized employee or agent of the purchaser, and date of signing;
5) Registration Number, Resale Number, or Certification of Resale to Out-of-State Purchaser
    A) purchaser's registration number with the Illinois Department of Revenue; or
    B) purchaser's resale number issued by the Department of Revenue; or
    C) a statement that the purchaser is an out-of-State purchaser who will sell only to purchasers located outside the State of Illinois.

Leasing

In regards to rental fees charged by clubs or golf courses for temporary use of the golf carts by patrons, please note that the State of Illinois taxes leases differently for Retailers' Occupation Tax and Use Tax purposes than the majority of other states. For Illinois sales tax purposes, there are two types of leasing situations: conditional sales and true leases.

A conditional sale is usually characterized by a nominal or one dollar purchase option at the close of the lease term. Stated otherwise, if lessors are guaranteed at the time of the lease that the leased property will be sold, this transaction is considered to be a conditional sale at the outset of the transaction, thus making all receipts subject to Retailers' Occupation Tax.

A true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See the enclosed copy of 86 Ill. Adm. Code 130.220. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. The State of Illinois imposes no tax on rental receipts. Consequently, lessees incur no tax liability.

The above guidelines are applicable to all true leases of tangible personal property in Illinois except for automobiles leased under terms of one year or less, which are subject to the Automobile Renting Occupation and Use Tax found at 35 ILCS 155/1 et seq.

As stated above, in the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid taxes in another state with respect to the acquisition of the tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state. See 86 Ill. Adm. Code 150.310(a)(3) enclosed.

Under Illinois law, lessors may not "pass through" their tax obligation on to the lessees as taxes. However, lessors and lessees may make private contractual arrangements for a

reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements.

Sale to Golf Courses/Clubs For Use as Utility/Turf Equipment

The Retailers' Occupation Tax Act imposes a tax upon persons engaged in the business of selling at retail tangible personal property. 35 ILCS 120/2 (1998 State Bar Edition). The Use Tax Act imposes a tax upon the privilege of using in this State tangible personal property purchased at retail from a retailer. 35 ILCS 105/3 (1998 State Bar Edition).

When a golf course or club purchases an item of equipment for use as utility or turf equipment, they are making a taxable use of the equipment. Therefore, tax is due on such sales.

Drop Shipment Scenario

A drop-shipment situation is one in which out-of-State purchasers (Purchasers) make purchases for resale from companies (Companies) which are registered with Illinois and have those Companies drop-ship the property to Purchasers' customers (Customers) located in Illinois. For this discussion, it is assumed that Purchasers are out-of-State companies that are not registered with the State of Illinois and do not have sufficient nexus with Illinois to require them to collect Illinois Use Tax.

As sellers required to collect Illinois tax, Companies must either charge tax or document exemptions when they make deliveries in Illinois. In order to document the fact that their sales to Purchasers are sales for resale, Companies are obligated by Illinois to obtain valid Certificates of Resale from Purchasers. See the enclosed copy of 86 Ill. Adm. Code 130.1405. Certificates of Resale must contain the following items of information.

1. A statement from the purchaser that items are being purchased for resale;

2. Seller's name and address;

3. Purchaser's name and address;

4. A description of the items being purchased for resale;

5. Purchaser's signature and date of signing;

6. Purchaser's registration number with the Illinois Department of Revenue; purchaser's resale number issued by the Illinois Department of Revenue; or, a statement that the purchaser is an out-of-State purchaser who will sell only to purchasers located outside the State of Illinois.

If Purchasers have no nexus with Illinois, it is unlikely that Purchasers would be registered with Illinois. If that is the case, and if Purchasers have no contact with Illinois which would require them to be registered as out-of-State Use Tax collectors for Illinois, then Purchasers could obtain resale numbers which would provide them the wherewithal to supply required numbers to Companies in conjunction with Certificates of Resale. We hope the following descriptions of out-of-State sellers required to register, either as Illinois retailers or as out-of-State Use Tax collectors and persons who qualify for resale numbers will be useful.

Assuming a delivery in Illinois, Illinois retailers are anyone who either accepts purchase orders in Illinois or who sells items of tangible personal property which are located in Illinois at the time of sale. See the enclosed copy of 86 Ill. Adm. Code 130.605(a).

Out-of-State sellers who fall under the definition of a "retailer maintaining a place of business in this State" (see 86 Ill. Adm. Code 150.201(i), enclosed) must register to collect Illinois Use Tax from Illinois customers and remit that tax to the Department. See 86 Ill. Adm. Code 150.801(c), enclosed. Please note that out-of-State sellers with any kind of agent in Illinois (not just sales or lease agents) are required to register as out-of-State Use Tax collectors. If Company B has no contact with Illinois, it does not fall within the definition of a "retailer maintaining a place of business in this State," and it need not register as an out-of-State Use Tax collector.

The United States Supreme Court in Quill Corp. v. North Dakota, 112 S.Ct. 1904 (1992), set forth the current guidelines for determining what nexus requirements must be met before a person is properly subject to a state's sales tax laws. The Supreme Court has set out a two-prong test for nexus. The first prong is whether the Due Process Clause is satisfied. Due Process will be satisfied if the person or entity purposely avails himself or itself of the benefits of an economic market in a forum state. Id. at 1910. The second prong of the Supreme Court's nexus test requires that, if due process requirements have been satisfied, the person or entity must have physical presence in the forum state to satisfy the Commerce Clause.

A physical presence does not mean simply an office or other physical building. Under Illinois tax law, it also includes the presence of any representative or other agent of the seller. The representative need not be a sales representative and it is immaterial for tax purposes that the representative's presence is temporary.

Resale numbers are issued to persons who make no taxable sales in Illinois but who need the wherewithal to provide suppliers with Certificates of Resale when purchasing items that will be resold. So long as Purchasers do not act as Illinois retailers and, so long as they do not fall under the definition of a "retailer maintaining a place of business in this State", their sales to Illinois customers are not subject to Illinois Retailers' Occupation Tax liability and they cannot be required to act as Use Tax collectors. So long as this is true, Purchasers qualify for resale numbers that do not require the filing of tax returns with the Illinois Department of Revenue. See 86 Ill. Adm. Code 130.1415.

Please note that the fact that Purchasers may not be required to act as Use Tax collectors for Illinois does not relieve their Customers of Use Tax liability. Therefore, if Purchasers do not collect Illinois Use Tax from their Customers, the Customers would have to pay their tax liability directly to the Illinois Department of Revenue.

While active registration or resale numbers on Certificates of Resale are still preferred, the Illinois Retailers' Occupation Tax Act provides as follows:

> "Failure to present an active registration number or resale number and a certification to the seller that a sale is for resale creates a presumption that a sale is not for resale. This presumption may be rebutted by other evidence that all of the seller's sales are sales for resale or that a particular sale is a sale for resale." 35 ILCS 120/2c.

Again, including registration or resale numbers from Purchasers on Certificates of Resale is the preferred method for documenting that their purchases from Companies are purchases for resale. However, in light of this statutory language, certifications from Purchasers on Certificates of Resale in lieu of resale numbers which described the drop-shipment situation and the fact that Purchasers have

no contact with Illinois which would require them to be registered and that they choose not to obtain Illinois resale numbers would constitute evidence that this particular sale is a sale for resale despite the fact that no registration number or resale number is provided. The risk run by Companies in accepting such a certification and the risk run by Purchasers in providing such a certification is that an Illinois auditor is much more likely to go behind a Certificate of Resale which does not contain a valid resale number and require that more information be provided by Companies as evidence that the particular sale was, in fact, a sale for resale.

Claim for Credit

If a taxpayer pays an amount of tax under the Retailers' Occupation Tax Act that is not due, either as a result of a mistake of fact or an error of law, the taxpayer may file a claim for credit with the Department. Only the persons remitting tax to the Department are authorized to file such claims. No credit shall be given the taxpayer unless the taxpayer shows that it has borne the burden of the tax or has unconditionally repaid the amount of the tax to the customer from whom it was collected. See the enclosed copy of 86 Ill. Adm. Code 130.1501. The claims for credit must be prepared and filed upon forms provided by the Department containing the information listed in Section 130.1501(b).

Under Illinois sales tax laws, retailers are not required to file claims for credit. Further, the Department has no authority to compel sellers to file a claim for credit. Whether or not sellers refund the taxes paid and file claims for credit with the Department is a private matter between sellers and purchasers.

Trade-ins

The Illinois Retailers' Occupation Tax Act imposes a tax upon persons engaged in this State in the business of selling tangible personal property to purchasers for use or consumption. The tax is measured by the seller's gross receipts from such sales made in the course of such business. See the enclosed copy of 86 Ill. Adm. Code 130.101. "Gross receipts" are considered to mean all the consideration actually received by the seller, except traded-in tangible personal property. See the enclosed copies of 86 Ill. Adm. Code 130.401 and 130.425. The tangible personal property must be taken by the seller in trade as all or part of the consideration for a sale. See Section 130.425(e).

No specific certification is required to document a trade-in. However, the retailer must maintain sufficient books and records to document such trade-ins. A purchaser may trade-in more than one item toward the purchase of another item or items from a retailer. Please note that the item or items to be traded-in must be of like kind and character as that which is being sold.

Record-keeping

Generally taxpayers are required to maintain business books and records during any period for which the Illinois Department of Revenue is authorized to issue a Notice of Tax Liability (NTL). See 86 Ill. Adm. Code 130.815, enclosed. As a general proposition, the Department can issue NTLs for 3 to 3 1/2 years. See Section 130.815(c), which explains how statutory periods expire in six-month intervals beginning with each January 1 and July 1. Consequently, taxpayers should retain appropriate records for at least 3 1/2 years. This assumes taxpayers are registered and filing returns with the Department.

We have enclosed Sections 130.801, 130.805, 130.810, 130.815, 130.820, and 130.825 of the Department's regulations for your information. An automated data process tax accounting system (ADP) may be used to provide the records required for the verification of tax liability. Such ADP

system must include a method of producing legible and readable records that will provide the necessary information for verifying such tax liability. The requirements apply to any taxpayer who maintains any such records on an ADP system and are set forth in detail in 86 Ill. Adm. Code 130.805.

If taxpayers retain records required to be retained under Section 130.801, in both machine-sensible and hard copy formats, the taxpayers shall make the records available to the Department in machine-sensible format upon request. ADP accounting systems encompass all types of data processing systems including, but not limited to, mainframe computer systems, stand-alone or networked microcomputer systems, Database Management Systems (DBMS) and systems using Electronic Data Interchange (EDI) technology.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.